No. 94-560

Supreme Court, U.S.
FILED
JAN 19 1995
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In The

Supreme Court of the United States

October Term, 1994

FIRST OPTIONS OF CHICAGO, INC.,

Petitioner,

v.

MANUEL KAPLAN, CAROL KAPLAN and MK INVESTMENTS, INC.,

Respondents.

On Writ of Certiorari To The United States Court Of Appeals For The Third Circuit

BRIEF OF *AMICI CURIAE* NATIONAL FUTURES ASSOCIATION, CHICAGO BOARD OF TRADE, AND CHICAGO MERCANTILE EXCHANGE IN SUPPORT OF PETITIONER

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I. STATEMENT OF INTEREST OF *AMICI CURIAE*

The Commodity Exchange Act, 7 U.S.C. §§ 1-22 (1994) – like the Securities Exchange Act of 1934 ("Securities Exchange Act"), 15 U.S.C. §§ 78a-78kk (1994) in connection with the regulation of the securities industry – sets forth a comprehensive system for the federal regulation of the commodity futures industry. *See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 355 (1982).

The Chicago Board of Trade ("CBOT") and the Chicago Mercantile Exchange ("CME"), which are futures exchanges, and National Futures Association ("NFA"), which is a registered futures association, are self-regulatory organizations ("SROs") authorized under the Commodity Exchange Act to resolve futures-related disputes through arbitration. *See* 7 U.S.C. § 7a(11) (1994) and 7 U.S.C. § 21(b)(10) (1994). In fact, futures SROs are required by law to arbitrate certain claims. *See Geldermann, Inc. v. Commodity Futures Trading Commission*, 836 F.2d 310 (7th Cir. 1987), *cert. denied*, 488 U.S. 816 (1988). Rules promulgated by the CBOT, the CME, and NFA must be submitted to the Commodity Futures Trading Commission ("CFTC") for approval pursuant to Sections 5 and 17, respectively, of the Commodity Exchange Act (7 U.S.C. § 7a(12) (1994); 7 U.S.C. § 21(j) (1994)) and must meet the standards set by CFTC Regulations §§ 180.1-180.5 (17 C.F.R. §§ 180.1-180.5 (1994)).

The arbitration forums administered by the CBOT, the CME, and NFA are very similar to the one at the Philadelphia Stock Exchange which was utilized by the parties in this case. The U.S. Supreme Court's holding in

this case would almost certainly be applied to arbitration cases filed with the futures SROs participating in this brief. Therefore, the CBOT, the CME, and NFA have a substantial interest in the outcome of the issues which the Court has chosen to review in this case.

The parties have consented to the filing of this *Amicus Curiae* brief by the CBOT, the CME, and NFA. Copies of the consent letters have been filed with the Clerk of the Court.

II. SUMMARY OF ARGUMENT

The CBOT, the CME, and NFA are filing this *Amicus Curiae* Brief in support of Petitioner, First Options of Chicago, Inc. These arbitration forums submit that the same deferential standard of review should apply to all issues actually submitted by the parties to the arbitrators for decision. Any less deferential standard is contrary to the intent of the Federal Arbitration Act (9 U.S.C. §§ 1-16 (1994)) and the national policy favoring arbitration of commodity futures and securities disputes.

Failure to apply a deferential standard of review to arbitrability issues submitted to and decided by the arbitrators could discourage arbitrators from serving and have other far-reaching effects on securities and commodity futures arbitration proceedings. Failure to apply a deferential standard of review will also encourage post-arbitration litigation and greatly reduce the advantages of arbitration, forcing claimants to either file their claims in court or forgo them altogether.

III. ARGUMENT

WHERE THE PARTY OBJECTING TO ARBITRAL JURISDICTION HAD SUBMITTED THE ISSUE TO THE ARBITRATORS FOR DECISION, A COURT REVIEWING THE ARBITRATION AWARD UNDER THE FEDERAL ARBITRATION ACT SHOULD APPLY THE SAME DEFERENTIAL STANDARD OF REVIEW TO THE ARBITRATORS' DECISION ON ARBITRABILITY THAT IT APPLIES TO THE ARBITRATORS' DECISION ON THE MERITS.

Amici have filed this brief to address a very narrow issue. This brief does *not* address the standard of review to be applied where the party challenging the arbitrators' jurisdiction did not submit that issue to the arbitrators for determination and participated in the arbitration proceeding only under protest. However, where the issue of arbitrability has been submitted to the arbitrators by the person challenging the arbitrators' jurisdiction over him, the arbitrators' decision should be subject to the same deferential standard of review that courts apply to the arbitrators' decision on the merits.

A. Failure to Apply a Deferential Standard of Review Could Discourage Arbitrators from Serving on Arbitration Panels and Have Other Far-Reaching Effects on Securities and Commodity Futures Arbitration Proceedings.

The *de novo* standard of review applied by the Third Circuit Court of Appeals allows courts to disregard the determinations of arbitrators on the arbitrability issue even where the parties had submitted the arbitrability

issue to the arbitrators for resolution. If this standard is upheld, a party who is unhappy with the result of the arbitration can get a second bite of the apple in court – relegating the arbitration award to an inferior status and wasting the often substantial time and energy expended by the arbitrators.

The typical arbitrator in an arbitration administered by a securities or futures SRO is a full-time lawyer or industry professional who serves with little or no compensation for the benefit of the industry and the investing public. These arbitrators are regularly called upon to resolve jurisdictional or arbitrability issues, and they devote substantial time and effort to the resolution of these issues. Where arbitrators resolve the jurisdictional issues in a case in favor of arbitrability, they continue to devote substantial time and effort to deciding the merits of the case.

If the reviewing court applies a *de novo* standard of review under these circumstances, the voluntary efforts of these skilled individuals to adjudicate arbitrability issues, which often involve questions of fact as well as law, will be fruitless. Substantial resources will be wasted, arbitrators will be deterred from serving on arbitration panels, and the arbitration process as a whole will be weakened. This result is contrary to the securities and commodity futures regulatory framework and to the liberal federal policy in favor of arbitration.

The resources expended on these cases is not limited to the arbitrators' time but includes the time and money spent by the parties and the arbitration forum on administering the arbitral process, providing a hearing facility,

procuring the attendance of witnesses, and hiring legal counsel. The potential waste of these resources and the increased difficulty in attracting the most qualified arbitrators could undermine the comprehensive arbitration systems currently in place in the securities and commodity futures industries, with far-reaching consequences.

Arbitration has become a common method for resolving disputes in the futures and securities industries. Over the five-year period from 1990 through 1994, the CBOT, the CME, and NFA alone received over 1,700 arbitration claims and disposed of over 2,000 cases, as follows:

Year	Entity	Total Cases Received	Total Cases Concluded
1990	CBOT	53	53
	CME	95	82
	NFA	278	454
1991	CBOT	50	49
	CME	90	81
	NFA	232	287
1992	CBOT	32	30
	CME	86	100
	NFA	200	303
1993	CBOT	69	44
	CME	60	76
	NFA	191	180
1994	CBOT	28	38
	CME	61	60
	NFA	189	180
TOTAL		1,714	2,017

The numbers in the securities industry are even more striking. Published information on arbitration cases at the seven largest securities industry SROs shows 24,229 cases filed and 24,261 cases concluded in the four year period of 1990-1993.

Year	Total Cases Received	Total Cases Concluded
American Stock Exchange		
1990	69	72
1991	51	64
1992	45	55
1993	48	55
Chicago Board Options Exhange		
1990	67	85
1991	46	62
1992	28	28
1993	15	18
Municipal Securities Rulemaking Board		
1990	75	90
1991	94	82
1992	45	68
1993	30	47

Year	Total Cases Received	Total Cases Concluded
National Association of Securities Dealers		
1990	3,617	4,019
1991	4,150	4,037
1992	4,379	4, 375
1993	5,419	4,327
New York Stock Exchange		
1990	1,378	1,466
1991	1,403	1,497
1992	873	1,167
1993	809	837
Pacific Stock Exchange		
1990	93	68
1991	86	82
1992	58	65
1993	199	54
Philadelphia Stock Exchange		
1990	29	34
1991	33	32
1992	21	18
1993	40	24

Year	Total Cases Received	Total Cases Concluded
	Total	
1990	5,701	6,423
1991	6,231	6,287
1992	5,737	6,189
1993	6,560	5,362

Source: 6 SECURITIES ARBITRATION COMMENTATOR, Oct. 1994, at 15; 5 SECURITIES ARBITRATION COMMENTATOR, Sept. 1993, at 9.

Similarly, the American Arbitration Association ("AAA") reports that 577 securities arbitration claims were filed there in 1991, 485 in 1992, and 635 in 1993. This is only a fraction of its overall filings, which totaled 63,171 in 1993. DISPUTE RESOLUTION JOURNAL, June 1994, at 5; ARBITRATION JOURNAL, March 1992, at 4. In fact, the claims and counterclaims in the 12,713 commercial cases filed at AAA in 1993 totaled over six billion dollars. Brief of American Arbitration Association as *Amicus Curiae* in Support of Petitioners, at Appendix, *Allied-Bruce Terminix Companies, Inc. v. Dobson*, 628 So. 2d 354 (Ala. 1993), *cert. granted*, ___ U.S. ___, 114 S. Ct. 1292 (1994) (No. 93-1001) (brief filed with the U.S. Supreme Court on May 18, 1994). *All* of these cases, as well as the thousands of other arbitration cases filed in other arbitration forums each year, are potentially affected by the standard of review applied to an arbitrator's determination of arbitrability.

In many of the cases which have been heard at futures, securities, and other arbitration forums, the arbitrators were presented by the parties with the question of

whether the dispute was arbitrable or whether the arbitration forum had jurisdiction over a party. It is unfair and wasteful to allow a party who unsuccessfully raises the issue of arbitrability before the arbitrators and thereafter participates in the entire arbitration proceeding (without seeking judicial relief or expressly reserving the right to do so) to subsequently reassert the arbitrability issue for *de novo* review by a court. This result is contrary to the national policy favoring arbitration in general and arbitration of securities and futures disputes in particular.

B. Failure to Apply a Deferential Standard of Review Could Encourage Litigation Over Arbitration Proceedings, Thereby Minimizing the Advantages of Arbitration, Increasing the Backlog in the Courts, and Depriving Some Claimants of a Forum for Resolving Their Disputes.

Although most arbitration forums do not keep statistics on the number of cases which involve arbitrability issues, our experience is that the numbers are significant. Obviously, it is much easier to overcome an arbitration award under a *de novo* standard of review than under a deferential standard of review. Therefore, the number of post-arbitration challenges to an arbitration award could increase substantially if the standard of review to be applied is *de novo* review rather than deferential review.

Arbitration is attractive because it tends to be quicker and less expensive than litigation. Anything that adds unnecessary length or costs to this process makes it less attractive and less cost-effective. As the number of post-arbitration challenges increases, so does the average length and expense of arbitration proceedings and the

probability that arbitration claims will end up in court. Claimants who believe that their claims will end up in court anyway because of a dispute over arbitrability are less likely to seek arbitration, with two possible results. Where the claim is large enough to justify the time and expense, some claimants may file their claims in court to begin with, thereby increasing the dockets and the backlog in the courts.[1] If these larger claims do end up in arbitration based on a pre-dispute agreement, the subsequent post-award litigation over arbitrability will have much the same effect on the backlog in an already overworked court system. Where the claim is for a smaller amount, as is typical for claims brought in securities and futures arbitration forums, claimants may simply decide to abandon their claims because those smaller claims cannot be pursued cost-effectively in any other forum. In either case, the result is inconsistent with the federal policy in favor of arbitration and the regulatory framework which promotes arbitration of claims in the securities and futures industries.

The claim in the underlying arbitration at issue here was for over $6,000,000, and the claimant in that case is a relatively large, well-capitalized firm which has the resources and the motivation to pursue its claim all the way to the U.S. Supreme Court. However, most arbitration claims are for much smaller amounts, and many

[1] *Amici* realize that most cases in the securities industry are governed by pre-dispute arbitration agreements. In the futures industry, however, a registrant may not require a customer to sign a pre-dispute agreement as a condition of doing business. 17 C.F.R. § 180.3 (1994). While some customers voluntarily sign these agreements, many do not.

involve claimants with limited resources. For example, of the 12,713 commercial arbitration cases filed with the AAA in 1993, 35% involved claims of $10,000 or less and 68% involved claims of $50,000 or less. Only 3% involved claims over $1,000,000. These smaller claims ($50,000 and under) took an average of 143 days (or 4.75 months) to resolve. Brief of American Arbitration Association as *Amicus Curiae* in Support of Petitioners, at Appendix, *Allied-Bruce Terminix Companies, Inc. v. Dobson*, 628 So. 2d 354 (Ala. 1993), *cert. granted*, ___ U.S. ___, 114 S. Ct. 1292 (1994) (No. 93-1001) (brief filed with the U.S. Supreme Court on May 18, 1994).

Statistics for the NFA and CBOT cases filed in the last two years show a similar concentration of smaller claims. In 1993, 52% of NFA's filings and 35% of the CBOT's filings involved claims of $10,000 or less; 72% of the cases filed at NFA and 45% of the cases filed at the CBOT involved claims of $50,000 or less; and 4% of the claims filed at NFA and 2% of the claims filed at the CBOT involved claims in excess of $1,000,000. For 1994, these numbers are 47% and 71%, respectively, for claims of $10,000 or less; 72% and 86% for claims of $50,000 or less; and 5% and 0 for claims over $1,000,000. Average turnaround times for claims of $50,000 or less during this same period ranged from a high of 7.75 months at NFA in 1994 to a low of 1.75 months at the CBOT in 1993. *Amici* are concerned that imposing a *de novo* standard of review on arbitrability issues will dramatically increase the time and expense required to resolve disputes through arbitration, effectively depriving customers with smaller claims of a forum for resolving their disputes.

IV. CONCLUSION

For all of these reasons, the Chicago Board of Trade, the Chicago Mercantile Exchange, and National Futures Association respectfully ask this Court to reverse the finding below and adopt the narrow holding that a court should apply a deferential standard of review to an arbitrator's decision concerning arbitrability if the parties had submitted that issue to the arbitrator for decision.

Respectfully submitted,

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